**The Promise and Perils of Empathy in Contracts**

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Legal sanctions, reputation costs, economic incentives, and social norms play a pivotal role in influencing behavior within contractual relationships. However, there are instances where individuals disregard breaches, even when such actions run counter to their economic interests and do not follow their contractual commitments or legal obligations. This article sheds light on a frequently overlooked motivator behind such behavior: contractual empathy.

The article delves into the capacity contracts to elicit empathy towards a struggling party who cannot fulfill its contractual obligations. It argues that in these cases, empathy can reduce litigation costs, facilitate cooperation and renegotiation, promote efficient and fair loss-sharing between parties, and increase social capital more generally. However, empathy also has its drawbacks, including fostering inefficient behavior in some cases, transferring wealth from empathetic to non-empathetic individuals, and reducing people’s well-being by experiencing negative emotions.

Empirical findings presented in the article provide initial insight into the extent empathy impacts behavior when one party is expected to breach the contract. These findings also highlight factors that moderate people’s willingness to disregard the breach including whether the promisor is an individual or a company and whether the contract is formally and legally negotiated.

The article concludes by discussing the legal implications of acknowledging empathy as a motivating factor in contractual settings.

**I. Introduction**

What influences behavior during contractual relationships? According to rational choice theory, people behave in a way that maximizes their benefits. Therefore, people will fulfill a contract if it serves their interests and enhances their welfare. From this perspective, legal sanctions and reputational considerations are the main incentives that influence how individuals perform their contracts.[[2]](#footnote-3) In contrast, expressive law theories emphasize the role of the law itself, beyond its effect via legal sanctions, in affecting people’s behavior.[[3]](#footnote-4) Applying these theories to the realm of contracts involves viewing contractual obligations and contract law as sources of motivation for action, either independently or through interaction with social norms. A third motive involves the moral aspects of keeping promises. This motivation can stem from a desire to fulfill commitments or to not disappoint others’ expectations.[[4]](#footnote-5)

 However, there are behaviors that cannot be fully explained by the motivations mentioned above. Consider, for instance, a contractor facing a severe health crisis that hinders the timely completion of home renovations. It stands to reason that at least some would refrain from demanding the agreed-upon penalties for the delay, opting instead to grant an extension. Others might go further by providing support to the contractor during his recovery. Similarly, imagine a single mother renting an apartment whose infant is injured in a car accident, requiring extended hospital stays. Consequently, she finds herself unable to meet her rent obligations. In such a situation, it would not be surprising if her landlord offered the option to defer payments and even considered waiving some of the payments during this challenging period.

These behaviors are arguably driven, at least partially, by a frequently overlooked motivator in the realm of contracts—empathy. Empathy is the ability to be sensitive to other’s experiences, thoughts, and feelings.[[5]](#footnote-6) People may feel empathetic toward strangers; however, the relationships that emerge through forming a contract, even in the context of a transactional contract and not a relational one,[[6]](#footnote-7) enhances this general empathy. In other words, it is more likely for the homeowner to support the contractor than a person unrelated to the situation. Similarly, the probability of a landlord waiving rent is greater than a stranger providing the single mother with the same amount. The key factor here is that the contract establishes a connection between parties, evoking a heightened sense of empathy or even a feeling of obligation stemming from this connectedness. Counterintuitively, the obligation felt by the homeowner and landlord toward the contractor and single mother, is not despite the duties they have toward them, but rather because of these duties. To some extent, they might feel that they are partially responsible for the difficulties the struggling party is facing and thus feel an obligation to alleviate this hardship. This sense of obligation, rooted in contractual relationships, is what we refer to as contractual empathy. Our focus in this paper is the effect of contractual empathy between a promisee and a promisor when the latter faces challenges in performing the contract.

Contractual empathy may prompt individuals to overlook breaches, extend deadlines, forgo entitled payments, and even incur losses to assist a party facing challenges. There are both benefits and pitfalls to contractual empathy. Firstly, contractual empathy averts adjudication of legal disputes, thereby eliminating litigation costs.[[7]](#footnote-8) Secondly, empathy promotes collaboration and eases the process of renegotiation, especially in situations where one party is anticipated to breach a contract, and the trust between the parties has been undermined.[[8]](#footnote-9) Contractual empathy also serves as a mechanism for sharing losses in a manner attuned to the financial circumstances of both parties, preventing insolvency and advancing fair and efficient allocation of losses resulting from unforeseen circumstances.[[9]](#footnote-10) Lastly, research predicts that considerate and altruistic actions will amplify social capital by fostering compassion, solidarity, and trust.[[10]](#footnote-11)

On the flip side, there are risks associated with contractual empathy. People might take imprudent risks, assuming the other party will come to their rescue if those risks materialize. Moreover, cynical parties may fabricate a dire situation to evoke empathy, encouraging inefficient behavior and leading to inequitable distributive outcomes.[[11]](#footnote-12) Additionally, considering that resources are limited, rational considerations may not support assisting those who evoke the most empathy, who are not always the ones who need the help the most.[[12]](#footnote-13) Finally, empathy leads to the experience of negative emotions that adversely affect people's well-being; therefore, all else being equal, this is something we may wish to circumvent.[[13]](#footnote-14)

To get initial insight into the extent empathy impacts contractual behavior and to assess possible moderating factors that influence empathetic behavior we ran two pre-registered studies. Both studies employ the same experimental paradigm. Participants are presented with a scenario where, due to COVID-19 restrictions, one party experiences economic difficulties and is unable to fulfill its obligation on time. The other party has three alternatives for how to respond. The first alternative, which we call *self-interest* behavior, involves insisting on receiving the agreed-upon liquidated damages, even if they exceed the damages incurred from the delay. The second alternative, *loss-avoidance* behavior, involves demanding compensation for the damages incurred. The third alternative, *loss-sharing* behavior, involves asking for compensation that does not fully cover the damages (or not asking for compensation at all).

As per the agreement between the parties, the promissee is entitled to receive all the liquidated damages. Additionally, the promissee is not a repeat player, and his reputation is not in jeopardy by demanding full compensation. Thus, in these circumstances, both the economic incentives and the legal requirements suggest that people will adopt a *self-interest* behavior. Moreover, even if people uphold contractual obligations due to the social norm of promise-keeping, they are not expected to forgo the full liquidated damages, which both parties agreed upon. Nevertheless, our findings imply that most people report that they will be satisfied with just receiving compensation for their loss, and some even engage in loss-sharing behavior.

In both studies, most participants did not request the strict enforcement of the contract and instead waived their right to receive full liquidated damages. These participants reported that they acted this way, even though most of them believed they would receive the entire liquidated damages if they went to court. A noteworthy minority (13%-14% of participants) stated that they would engage in loss-sharing behavior and absorb some of the loss incurred by the breach. However, most of these participants did not think that their actions should be mandated by law. As expected, the behaviors exhibited were significantly associated with the level of empathy that participants felt towards the breaching party.

In Study 1, it was demonstrated that people’s behavior is influenced by the identity of the contracting party. When the struggling business was presented as a person named Jennifer, the participants were significantly less focused on economic maximization and more inclined to be loss-sharing than when the business was portrayed as a company. Study 2 found that eliciting empathy towards the struggling party led to participants being less focused on economic maximization. Additionally, when the contract was crafted in a formal and legal manner, participants were more inclined to maximize their compensation and less likely to exhibit loss-sharing behavior.

While these vignette studies do not aim to mirror the exact incentives at play in real-life events, they do demonstrate the significance of contractual empathy in shaping behavior in such situations. Given empathy’s role in contractual behavior, we must take it into account when shaping legal policies.

In terms of normative considerations, two key inquiries arise. Firstly, should we harness the expressive function of contract law to amplify contractual empathy? We contend that determining the optimal level of empathy is not straightforward. Caution is warranted when navigating emotions and preferences, given the obscured nature of the desired outcomes. Moreover, we emphasize that widespread empathy may institutionalize empathetic behavior as a social norm. While potentially beneficial, this also creates a near-obligatory adherence. The desirability of this outcome is linked to the second inquiry—should we introduce more obligatory regulations mandating considerate conduct, or conversely, ease pro-social requirements? We posit that despite potentially narrowing the behavioral gap between empathetic and non-empathetic individuals, this approach is problematic. Firstly, many benefits associated with empathy derive from its voluntary nature; imposing compassion mandates in contracts may yield inadvertent consequences. Secondly, demanding and enforcing pro-social behavior could trigger a crowding-out effect, leading to decreased considerate behavior due to the obligatory rules.

The article proceeds as follows. Part II discusses the diverse motivations influencing contract behavior, specifically empathy. Part III explores the advantages and potential risks of contractual empathy. Part IV introduces and analyzes our empirical findings. Part V delves into the normative implications arising from the presence of contractual empathy. Lastly, Part VI concludes and provides guidance for future research.

**II. Contractual Behavior and Empathy**

Stewart Macaulay’s influential 1963 paper, convincingly demonstrated that individuals frequently do not insist on enforcing their contractual rights and disregard breaches. This has been classically explained by the value people place on preserving trust in long-term contractual relationships, especially in closed business communities,[[14]](#footnote-15) as well as the importance of maintaining a positive reputation among repeat players.[[15]](#footnote-16)

 An additional explanation for this phenomenon may go beyond self-interest incentives. Many experiments have shown that people deviate from purely economic behavior in *trust games*. In a trust game, one player is given a sum of money which they can choose to transfer to the other player. The amount transferred is then multiplied by a certain factor, and the second player can decide whether to return some of the money to the first player. From a rational choice perspective, the first player should transfer nothing, as a self-interested second player will not return any money. However, multiple experimental studies have shown that people do transfer money as “player 1” and return some of the money as “player 2.”[[16]](#footnote-17) This indicates that people often act in a trustworthy manner even without any enforcement mechanism. Moreover, a study by Garry Charness and Martin Dufwenberg found that conveying an unenforceable promise from player 2 to player 1 (what economists would call “*cheap talk*”) significantly increases cooperation between the players.[[17]](#footnote-18) This suggests that contracts, which serve to communicate promises, can facilitate trust and cooperation even without mechanisms of enforcement or reputation.

This behavior could be attributed to the inherent value people place on keeping promises. Even if promises are unenforceable, people feel a moral obligation to fulfill them, as breaking this norm leads to guilt that they would like to avoid.[[18]](#footnote-19) Another explanation stems from the desire to avoid falling short of the expectations of others.[[19]](#footnote-20) Although expectations alone may not necessarily create commitment, after an individual makes a promise to someone, she feels obligated to meet the other person’s expectations. This may be due to the belief that the promisor generated these expectations or due to the personal connection that the promise established.[[20]](#footnote-21) Moreover, the personal connection created by a promise, or a contract also enhances trust and cooperation in general and affects the expectations of the other party. According to David Hoffman & Tess Wilkinson-Ryan, when a promisee perceives his or herself as being in a contractual relationship, he or she tends to exercise less caution. Through a series of studies, they revealed that individuals are more inclined to safeguard their own interests, such as requesting a liquidated damages clause, purchasing a warranty, or shopping around for the best deal, when the contract is not yet concluded, as opposed to when they believe the agreement is final.[[21]](#footnote-22)

The moral commitment to perform contractual obligations cannot explain a behavior of overlooking breaches. When faced with norm violations and breaches, trust is diminished, and legal sanctions are expected.[[22]](#footnote-23) However, if entering a contract creates a personal connection between the parties, it may in turn cause them not to insist on their contractual rights. More specifically, the personal connection established through the contract may lead the promisee to empathize with the promisor’s situation and refrain from strictly enforcing the contract, regardless of any expectations.

As mentioned above, empathy is the ability to be sensitive to other’s experiences, thoughts, and feelings. Research indicates that empathy drives individuals to engage in prosocial behavior and provide support to those in need.[[23]](#footnote-24) Various situations elicit varying levels of empathy, consequently promoting prosocial behavior to different extents. The intensity of negative emotions arising from a situation, coupled with the degree of similarity between the observer and the individual experiencing it, also influences the observer’s reaction.[[24]](#footnote-25) The nature of the relationships among the parties involved further shapes their responses. It is expected that empathy between romantic partners or friends would be higher compared to that between strangers.[[25]](#footnote-26) Similarly, empathy towards a situation in a distant country differs from that in proximity.[[26]](#footnote-27) Thus, individuals who are bound to each other by a contract are also expected to develop a sense of empathy between them, which becomes evident when encountering challenging situations—an aspect not as pronounced between strangers.

When one party experiences difficulties in fulfilling a contract, the other party’s behavior may be influenced by the empathy created. Imagine a dedicated kindergarten teacher who also owns and manages the kindergarten. Due to the sudden and tragic death of her son, she finds herself unable to open her kindergarten for a month. This unforeseen personal crisis prevents her from providing the expected services to the parents and children under her care. It seems that even in the absence of any legal obligation to pay for the unprovided services during this period, some parents will voluntarily decide to continue, at least partially, paying tuition. Their decision goes beyond the strict terms of the contract, demonstrating a genuine sense of empathy and solidarity in supporting the other party.[[27]](#footnote-28) As mentioned in the introduction, this empathetic obligation is distinct from general compassion and is created by the contract. Contracts are not only the source of legal duties but also of compassionate duties. The fact that the teacher has an obligation toward the parents morally binds the parents when the teacher faces challenges in connection to the contract. The parents are anticipated to feel more responsible for the teacher’s situation, to be more empathetic toward her, and consequently act altruistically by paying her.[[28]](#footnote-29)

While the law may at times include the principles of mutual consideration and compassion into the parties’ obligations, it is not always the case.[[29]](#footnote-30) The excuse doctrine encompasses diverse principles that allow parties to be released from a contract in exceptional and unforeseen cases that fundamentally alter the nature of the parties’ agreement, this includes the impossibility, impracticability, and frustration doctrines.[[30]](#footnote-31) However, the exact threshold for identifying such exceptional cases is vague, and parties are generally expected to fulfill their contractual obligations even if it becomes more challenging than anticipated.[[31]](#footnote-32) Nonetheless, despite no rule requiring individuals to waive their contractual rights, they may still feel compelled to act compassionately towards a struggling party.

The extent and manner in which empathy influences behavior in the face of breaches depend on several factors related to the specific context of the situation. These factors include, for example, the nature of the relationship between the parties, the motivation and fault that behind the breach, whether the other party was informed of the breach in advance, and whether the breaching party is an individual or a company.[[32]](#footnote-33) Thus, if the breaching party is an individual and the breach is due to unforeseen circumstances outside of their control, individuals may be more understanding and willing to work towards finding a solution. On the other hand, if a company intentionally breached the contract and did not provide advance notice, individuals may be less lenient and more inclined to pursue legal recourse. Overall, the way in which individuals respond to breaches in a contractual situation can be complex and multifaceted.

**III. Benefits and Risks in Contractual Empathy**

Contracts founded not only on self-interests and legal commitment but also on empathy encompass both advantages and potential pitfalls, influencing both overall social welfare and distributive objectives. This chapter reviews the benefits and risks inherent in contractual relationships infused with empathy.

***Litigation costs.*** Empathy’s impact on social welfare is notably manifested in the realm of litigation costs. The empathetic connection between the promisee and the struggling promisor can lead to a considerate response, wherein the breach is either overlooked or the promisee willingly absorbs some of the resulting losses. Consequently, this empathetic behavior makes it more likely for the promisor to fulfill remaining obligations, thus reducing the probability of resorting to legal proceedings. Even in situations where the promisor believes she is justified in breaching the contract, the inclination to pursue litigation is curtailed. This reduction in litigation propensity can be attributed to two key factors. First, the promisor, not having absorbed all the losses, finds the potential benefits of litigation reduced. Second, in the face of the promisee’s goodwill, the promisor may reciprocate in kind and forego stringent insistence on perceived rights. To illustrate, consider the kindergarten teacher who, having endured a tragic event, feels entitled to a month’s leave with full pay. However, the parents, displaying empathy, willingly offer to pay half the tuition. In such a scenario, the teacher might opt against legal action, either due to uncertainty about prevailing in court or out of appreciation for the parents’ willingness to cover half the expenses.[[33]](#footnote-34)

***Increased Cooperation.*** Facilitating cooperation is another dimension where empathy can enhance the overall social welfare arising from a contract. Cooperation often results in an increased joint surplus for both contracting parties. In the context of contracts, cooperation hinges on the assumption that both parties adhere to their contractual obligations. When faced with a breach, the promisee has two general response options: insistence on the promisor’s obligations with subsequent legal sanctions, or a more empathetic approach, involving the waiver of some legal rights. While imposing legal sanctions may bolster future cooperation through deterrence, waiving rights can foster cooperation through reciprocal goodwill. Research suggests that employing costly punishments in cooperation games tends to reduce the joint surplus compared to strategies that abstain from such punitive measures.[[34]](#footnote-35)

Ample research suggests that empathy could enhance cooperation by allowing parties to overcome misunderstandings between them which could sometimes hinge on the likelihood of cooperation.[[35]](#footnote-36) Research on social cooperation predicts that empathy has the potential to improve the goodwill of parties to the contract and consequently the efficacy of contracts, given how frequent are cases of uncertainties, especially in long-term contracts.[[36]](#footnote-37)

However, persistently demonstrating goodwill in the face of defection from cooperation may also be an ineffective strategy for the cooperating party.[[37]](#footnote-38) Interestingly Batson who is one of the leading scholars to support the benefits of empathy to society and social interactions[[38]](#footnote-39) was also one of the early voices to recognize that it might become counterproductive when the target of empathy is exploiting trust and defect.[[39]](#footnote-40) Finally, we know from other studies, how important it is to have the ability to punish others for lack of cooperation,[[40]](#footnote-41) to allow for effective social cooperation to work, and we can safely assume that excessive empathy towards a person who breaks his promise and the attempt to avoid conflict and confrontation at any cost, is likely to harm the likelihood of cooperation.[[41]](#footnote-42)

***Facilitates renegotiation.*** If both parties possessed full information and crafted a complete contract, accounting for all potential future contingencies and factors impacting the parties**—**we could presume the contract’s efficiency. However, in reality, unforeseen events may unfold, rendering the existing contract inefficient. For instance, imagine a homeowner ordering a product with a $20 damage cost for any delay, while the provider’s estimated cost for timely delivery is only $10. In such a scenario, the provider might agree to include a $20 liquidated damages clause for a potential delay. Yet, unexpected events can alter the circumstances; if the homeowner’s damage from a delay decreases to $10, and the provider’s cost for timely delivery rises to $15, adhering strictly to the original contract becomes inefficient. Ideally, renegotiation should allow for adjustments that benefit both parties by optimizing the joint surplus. A rational choice perspective suggests that, even without empathy, renegotiation is likely, and the parties will reallocate the gains from the contract. However, renegotiation can be cumbersome, especially in the face of an expected breach. When empathy is present, offering a willingness to absorb some losses incurred by the other party increases the likelihood of successful renegotiations.

***Efficient and fair loss sharing.*** *Ceteris paribus,* it is preferable that parties will share fairly losses resulting from unforeseen events. Determining a fair distribution of losses is a complicated process, influenced by factors such as the parties’ expected gains from the contract, their responsibility in foreseeing unexpected events, and their relative wealth. Beyond the normative aspect of determining a fair distribution, there is a factual dimension that the parties, possessing intimate knowledge of the situation, are better suited to navigate than the courts. When the promisee is driven by empathetic concerns and willingly participates in fair loss sharing, the likelihood of achieving fairness in distribution is heightened compared to relying on legal proceedings. Additionally, from a perspective of distributive justice, empathy is expected to do better in terms of redistributing wealth. A poor party will not bear the burden of losses when the wealthier party encounters difficulties fulfilling the contract. Consequently, parties, who possess more information than the court on the relevant circumstances, are more adept at fostering a fair and equitable distribution of wealth.[[42]](#footnote-43) Furthermore, the normative complexities inherent in determining how to share losses become more manageable when the sharing is voluntary.

Moreover, the issue of loss sharing extends beyond mere distribution; it also significantly impacts total social welfare. When one party faces financial distress and is on the brink of insolvency, sharing some of the losses by the other party to aid in the struggling party’s survival may increase social welfare. For instance, allowing parents not to pay a teacher during her leave may lead to the kindergarten’s bankruptcy, impacting both the parents and the teacher. In cases where it is in the mutual interest of both parties for the institution to remain operational, successful renegotiation can still result in an efficient sharing of losses. However, when the party who has adequate alternatives is not legally obliged to share losses, legal rules may fall short in addressing this issue. Courts lack the necessary knowledge to determine the most efficient way to allocate losses. In contrast, empathy motivates the promisee to assist the struggling promisor only when needed since individuals are inclined to help when the costs are modest and the benefits for the other party are significant.[[43]](#footnote-44) Consequently, loss-sharing through empathetic actions is likely to yield a more efficient distribution of losses.

Interestingly, Yehonatan Givati, Yotam Kaplan, and Yair Listokin have posited that the legal uncertainty associated with the excuse doctrine can create incentives for loss-sharing among different classes of contractual parties, ultimately minimizing the costs of prolonged economic instability.[[44]](#footnote-45) An illustrative example unfolded during the COVID crisis, wherein the excuse doctrine facilitated an extraordinary surge in contractual renegotiation and loss sharing without triggering excessive litigation. Alternatively, one could interpret this phenomenon as arising from the widespread challenges posed by COVID-19, fostering a heightened sense of empathy. Faced with an unexpected and universally impactful event, individuals may have been more inclined to participate in renegotiation to ensure fair and efficient loss sharing.

However, the optimistic perspective on how empathy facilitates fair and efficient loss sharing is jeopardized by the potential for deceptive claims of need. Recognizing that individuals are responsive to empathy and are inclined to share losses in the event of unforeseen circumstances, there is a risk that individuals may feign dire situations. In such instances, empathy has the potential to result in inefficient and unjust loss-sharing.

***Social capital.*** The literature in the realms of social influence[[45]](#footnote-46) and reciprocity[[46]](#footnote-47) suggests that pro-social behavior arising from empathy can impact not only the parties involved in the contract but also society at large. Empathy extends not only to the future interactions between the parties in the current contract but also spillovers to various other interactions of the struggling party’s future relationships with others.[[47]](#footnote-48) Altruistic and empathic actions also contribute to the growth of social capital by nurturing compassion,[[48]](#footnote-49) solidarity, [[49]](#footnote-50) trust,[[50]](#footnote-51) and honesty.[[51]](#footnote-52) Such a high social capital society is likely to be a society with greater social cohesion, greater engagement in civic actions, inclusive social institutions, and with stronger social network. The main process through which greater compassion in contract could spill over to society is through reciprocity which will lead to a change in the social norms regarding contracts. Parties to a contract who experience that when they were faced with hardship, the other party to the contract attempted to accommodate their needs, are likely to reciprocate and behave similarly to others who will face similar situations.[[52]](#footnote-53)

***Incentives to an inefficient behavior.*** When a party is aware that breaching a contract would entail paying damages equivalent to the harm caused by the breach, there is an incentive to invest a comparable amount in preventing the breach from occurring. Alternatively, the party may decide not to enter the contract at all if the anticipated damages to be paid would surpass the profit expected from the contract. However, if a promisor understands that in the event of a breach, he will not bear the full consequences due to empathetic loss sharing, there is a risk of underinvestment in precautionary measures to avert the breach. Also, it could lead to entering an inefficient contract where the risk of a breach outweighs the benefits, resulting in a negative surplus.

Similar fears have been raised regarding bankruptcy law in general[[53]](#footnote-54) and government bailouts for companies that are too big to fall. This is in a way an example of a much larger problem that is associated with the moral hazard problem in law and economics scholarship.[[54]](#footnote-55) If a corporation or in our context, contractual parties know that there is a greater chance that if they face difficulties, the other party to the contract will forgive them, they might be encouraged to take too many risks, which they will not fully internalize themselves.[[55]](#footnote-56)

Indeed, the voluntary nature of empathetic behavior provides individuals with the flexibility to discern irresponsible conduct. Consequently, when the promisee perceives that the promisor has taken unreasonable risks, she will be less inclined to help. Nonetheless, even if the promisee understands that the promisor took imprudent risks, he might still be willing to share the losses due to empathy.

Another inefficient behavior arising from empathetic loss-sharing occurs when individuals breach contracts even when such actions are inefficient. For instance, leveraging the generosity of the parents, a teacher may choose to take more than a month off, secure in the knowledge that she will still receive payment despite the breach of contractual obligations. This behavior, driven by the expectation of empathetic compensation, may lead to suboptimal outcomes and undermine the efficiency of contractual relationships.

Finally, empathy can sometimes turn to be inefficient in doing business, given the problem of mixing money and love in economic activity.[[56]](#footnote-57) The combination of money and love is seen in economic literature as harming the ability to stay objective in evaluating business performance of friends with whom you do business. In addition, friends might avoid alerting the other side to misbehavior because of the fear of harming the relationship. In addition, in many situations where people have some duty to oversee the performance of other parties to a business endeavor, they might be in some ethical conflict of interest because of some special type of friendship or emotional connection. While in the context of empathy in contracts we are not talking about love or friendship, one might speculate that problems might be in the same direction albeit on a weaker magnitude.

***Non-empathetic people prosper.*** A prominent drawback of relying on empathy for loss-sharing is that only empathetic individuals are likely to engage in such behavior. Consequently, over the long term, this practice may result in transferring wealth from empathetic individuals to those lacking empathy. Empathetic behavior, as discussed earlier, can be advantageous to the empathetic person by fostering cooperation, encouraging renegotiation, and potentially yielding positive effects. Nevertheless, in many instances, empathetic individuals may find themselves transferring wealth without receiving anything in return beyond the satisfaction of positive emotions.

In some cases, variations in the level of empathy can directly result in cross-subsidization. Consider a company aware of a 10% chance that it will not perform its contract. In case of a breach, the company expects to pay compensation of $100 for 50% of the customers, while the other 50% are anticipated to be empathetic and content with $50 in compensation. In this scenario, the company is likely to increase prices for all customers by $7.5, allocating $5 to cover damages for non-empathetic parties and only $2.5 to cover damages for empathetic parties.[[57]](#footnote-58)

***Selective and inefficient charitable behavior.***Paul Bloom in his powerful book,[[58]](#footnote-59) largely suggests that empathy is a very problematic emotion to base public policy on. While some of his arguments are related to policy decisions made by states rather than by parties to a contract, some of the arguments he made in the book, seem highly relevant to our contexts. First, empathy could be highly affected by various biases such as the identified victim effect[[59]](#footnote-60) or ingroup bias.[[60]](#footnote-61) This suggests for example that if we encourage reliance on empathy in contracts, we might create a situation where people might demonstrate more empathy towards contractual parties who are easier to identify with or with people who look like them.[[61]](#footnote-62)

***Negative emotions.*** Our discussion has primarily focused on how empathy influences behavior in contractual situations. However, one needs to also consider the negative emotional impact on individuals who express empathy, especially in the context of social welfare. Empathy, while beneficial, can sometimes be a source of distress for the empathizer. This aspect of empathy can be viewed as a social cost, a perspective supported by scholars like Gilbert and Hayashi.[[62]](#footnote-63)

Importantly, the negative influence of empathy on emotions is inherently tied to the behavior of the involved parties. For example, consider a case where a promisee empathizes with a promisor, yet they are unable to reach a mutual agreement, leaving the promisor dissatisfied with the proposed solution. In such cases, the initial empathy felt by the promisee might gradually weaken. This erosion of empathy can become more pronounced if the conflict escalates to legal proceedings, where the formal and adversarial nature of the setting can further dampen empathetic feelings. On the other hand, if a resolution is found – such as the promisor accepting the promisee's proposal to share the losses – the promisee's feelings may evolve from sympathy towards the promisor to a sense of fulfillment derived from providing assistance. This dynamic nature of empathy, and its varying impact depending on the interaction outcomes, adds layers of complexity when considering empathy as a factor in the social welfare equation.

Furthermore, an alternative perspective may not perceive the negative emotions stemming from empathy as a cost, but rather value the presence of empathy in society for its intrinsic worth, independent of its direct contributions to social welfare. Consider, for instance, a world where parents who lose a child in an accident feel no sorrow due to a lack of empathy. Is an emotionless society like this desirable? Many would argue against the idea of a world stripped of such fundamental human emotions, underscoring the inherent value of empathy that transcends its tangible impact on social welfare metrics.

Our objective here is not to determine which of these perspectives is more valid, but to highlight the importance of considering these differing viewpoints when developing policies that might affect empathy levels in society.

In this section, we investigated the risks and benefits associated with contractual empathy when one party encounters challenges in fulfilling the contract. But to what extent does this phenomenon occur, and how does it influence people’s propensity to empathize with the other party and subsequently alter their behavior? The following section offers preliminary findings that contribute insights to these questions.

**IV. Experimental Investigation**

We had three general hypotheses. First, in situations where a party is experiencing economic hardship that makes it difficult for it to fulfill its contractual obligations, most people will not act in a self-interested manner. Second, many people will act charitably and absorb some of the losses caused by the breach, without requiring compensation. Finally, the level of empathy that one feels towards the struggling party is expected to be associated with these behaviors. In the following section, we present two studies designed to test these hypotheses, as well as explore various factors that may influence people’s behavior in such situations.

To explore empathetic behavior in contractual relationships we conducted a series of studies employing a similar experimental paradigm. Participants were presented with a vignette describing a party that due to economic difficulties asked to delay a delivery and thus breach the contract. The other party, John, had three alternatives to respond to this situation. First, he could insist on the delivery on time, or get compensation that would exceed the damages he would incur due to the delayed delivery, what we dubbed as *self-interest* behavior. Second, he could demand compensation that will compensate for the damages he will incur from the breach, a *loss-avoidance* behavior. Finally, a third option is to employ a *loss-sharing* behavior by agreeing to take some of the damages upon himself, and not to be fully compensated for them. John is not a repeat player, and his reputation is not in jeopardy by demanding full compensation. Thus, the two latter behaviors may be considered altruistic, and seemingly not driven by legal obligations or self-interest motives. The following studies are thus aimed to show the extent of altruistic behavior in different contexts, its connection to empathy, and how different factors elicit this type of behavior.

***a******. Study 1: The Effect of Empathy and Contracting Party on Behavior Toward the Struggling Party.***

The objective of our study was to investigate methods for eliciting altruistic behavior in cases of contract breach. Since this behavior goes beyond the norm of keeping promises, we hypothesized that it would primarily stem from the level of empathy that the promisee feels towards the struggling party. Thus, in this study we manipulated the level of empathy the promisee feels towards the breaching party to test the effect of empathy on behavior. Additionally, we examined the impact of the type of contracting party on the promisee’s behavior. Previous research by Uriel Haran suggested that contracts involving individuals are more closely associated with promises than those involving organizations.[[63]](#footnote-64) Thus, breaching a contract with an individual is seen as a moral transgression, and the same behavior by an organization is viewed as a legitimate business decision. This gap is aligned with rich literature that shows how people differentiate in the empathy they have towards corporations and individuals.[[64]](#footnote-65) At the same time some literature shows that although people are well aware that corporations are highly unlike individuals, they still have emotions toward them and their actions, and perceive their behavior to be intentional and internally driven.[[65]](#footnote-66) Furthermore, researchers have also found that people’s impressions of corporations are formed based on the same principles that guide their impressions of persons’ warmth and competence. Warmth judgments include perceptions of generosity, kindness, honesty, sincerity, helpfulness, trustworthiness, and thoughtfulness, whereas competence judgments include confidence, effectiveness, intelligence, capability, skillfulness, and competitiveness. Generally speaking, it was shown for example that non-profit organizations were seen as less competent but with higher warmth than for-profit organizations.[[66]](#footnote-67) Thus, when comparing corporations to people, it is expected that the gap in perceived warmth will also translate into a gap in empathy, as identified in a series of findings by Tang & Gray.[[67]](#footnote-68)

Based on this literature, we hypothesized that people would display more altruistic behavior towards individuals due to the moral considerations inherent in such contractual relationships while exhibiting less altruistic behavior towards companies, which are typically viewed as business deals driven mainly by economic considerations.

**1. Participants**

Two hundred and three participants from the United States were recruited through the crowdsourcing company, Prolific, and completed a pre-registered questionnaire online.[[68]](#footnote-69) Twenty-nine participants who failed the attention check were excluded from the analysis. Of the remaining 174 participants, 91 were male, and 83 were female. The average age was 36.84 (SD = 13.65), 112 participants had some academic education, and the average Political Worldview score (on a scale from *0 = liberal*, to *100 = conservative*) was 36.48 (SD=27.19).

**2. Procedure**

Participants were presented with a vignette describing a transaction where John ordered light fixtures from a small business to replace his existing ones. According to the agreement, the light fixtures should be delivered by April 30, 2020, and in case of a delay in the delivery, John should be compensated by $1,000. After the deal, the COVID-19 pandemic began to spread, and the restrictions caused an expected two-week delay in the delivery of John’s light fixtures. Since the contractor who renovated John’s house is supposed to finish working for John by the end of April, the delay in delivery will result in additional costs of $500 for the light fixtures installment.

The study design included two independent variables in a 2X2 between-subject format. The first variable was *empathy elicitatio*n, where half of the participants simply read the vignette as presented (*control group*), while the other half were informed about the business’s recent history of delayed orders, customer complaints, and compensation demands, putting the business in danger of closing and causing job loss for employees (*empathy* *elicitation* condition). The second independent variable was the type of contract parties, where half of the participants were told that Jennifer was the owner of the small business and all interactions were between Jennifer and John (*individual* condition), while the other half were informed that the business was referred to as Light Fixtures Inc. and the owner was not mentioned (*company* condition).

Participants were initially posed three questions to test their comprehension. They were then asked to put themselves in John’s situation and choose one of three options: (1) demand either an expedited delivery or the agreed compensation of $1,000 (or more than $500); (2) ask for compensation of $500 for their loss; and (3) accept not being compensated for the full loss (less than $500). They were also asked to predict what the outcome *will* be if the case would go to court, and what the judgment *should* be. The participants then rated, on a scale of 1 to 7, whether behaviors (1) and (2) above are immoral, and the extent to which they should be viewed as reasonable business behavior. They also indicated their agreement with three statements designed to gauge their empathy for the small business. Finally, the participants provided some demographic information (for the full text see Appendix A1).[[69]](#footnote-70)

**2. Results**

Only 42% of the participants demanded compensation of above $500 or insisted on expedited delivery. Forty-five percent of participants demanded compensation that would cover their losses, and 13% agreed to be only partly compensated or not compensated at all. To test the impact of empathy and the contracting party on behavior, we created two dummy variables: (1) *Self-interest* which is assigned a value of 1 when participants express a desire for either an expedited delivery or compensation exceeding $500, and 0 in all other cases; (2) *Loss-sharing* which is assigned a value of 1 when participants indicate a willingness to accept less than $500 in compensation, and 0 in all other cases.

 To test the association between empathy and contract behavior we regressed both *Self-interest* and *Loss-sharing* on *empathy elicitation*. No significant effect was found (p=0.36 in both logistic regressions) suggesting that our attempt to elicit empathy to encourage solidarity failed. Moreover, no significant association was found between the empathy participants felt toward the small business—as measured by the three-statement scale (α=0.81)—and the *empathy elicitation* condition. This implies that our elicitation did not evoke empathy. However, as shown in Table 1, empathy as measured by the scale was highly significantly associated with both *Self-interest* (negatively) and *Loss-sharing* behavior (positively).

 An association was also found between the contracting party and behavior, whereby when the small business was portrayed as Jennifer as opposed to Light Fixtures Inc., participants were more solidaristic (see Figure 1). Logistic regressions depicted in Table 1 demonstrated a significant association between the contracting party and *Self-interest* even after controlling for demographics, and no significant association between the contracting party and *loss-sharing*. Additionally, no interaction effects of the contracting party and empathy condition on either *Self-interest* or *Loss-sharing* were found. In addition, under the *individual* condition, participants reported significantly more empathy toward the business (r=0.19, p=0.01).

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| **Table 1:** *Logistic Regression Analysis of The Effect of Empathy and Contracting Party on Behavior in Study 1* (N=174) |
|  | **DV: *Self-interest***  | **DV: *loss-sharing***  |
|  | **M1** | **M2** | **M3** | **M1** | **M2** | **M3** |
| Empathy Scale | -0.47\*\*\* |  | -0.42\*\* | 0.65\*\* |  | 0.66\*\* |
| Company |  | 0.83\*\* | 0.7\* |  | -0.76 | -0.64 |
| Political Worldview |  |  | 0.01 |  |  | 0.01 |
| Academic Training |  |  | -0.33 |  |  | 0.07 |
| Age  |  |  | -0.2+ |  |  | 0 |
| Female |  |  | 0.19 |  |  | -0.13 |
| **R2** | 0.07 | 0.03 | 0.1 | 0.07 | 0.02 | 0.1 |
| + *p* < 0.1. \* *p* < 0.05. \*\* *p* < 0.01. \*\*\* *p* < 0.001. |

 As shown in Table 2, the majority of those who reported loss-avoidance and loss-sharing behavior stated that they thought they were not obligated by law to behave in such a manner (55% and 86% respectively). Moreover, a substantial portion of individuals exhibiting loss-avoidance (32%) and a majority of those displaying loss-sharing behavior (64%) believed that their actions should not be mandated by law.

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| **Table 2:** *Participants Reported Behavior by Their Expected Judgment and Personal Attitude in Study 1* (N=174) |
|  | **Expected Judgment** | **Desirable Judgment** |
|  | **S.I.** | **L.A.** | **L.S.** | **S.I.** | **L.A.** | **L.S.** |
| **Self-interest** | 84% | 16% | 0% | 82% | 16% | 1% |
| **Loss-avoidance** | 55% | 42% | 3% | 32% | 65% | 3% |
| **Loss-sharing**  | 27% | 59% | 14% | 14% | 50% | 36% |

**4. Discussion**

These results demonstrate that most participants exhibit altruistic behavior by refraining from demanding compensation that would leave them better off than if the contract had been fulfilled without any delays. Among these participants, 62% acted in this way even though they believed they could receive greater compensation through legal means. Furthermore, 13% of the participants stated that they would behave in a loss-sharing manner in such a situation, foregoing full compensation for any damages incurred.

 Although a significant association was found between the empathy people had toward the struggling party and their behavior, the empathy manipulation did not have such an impact on behavior. However, it is hard to derive any meaningful insights from this null effect, since we did not find a significant association between empathy elicitation and the actual reported empathy, suggesting our manipulation did not necessarily evoke empathy as envisioned. Conversely, the identity of the contracting party did influence participants’ behavior, with those who contracted with a company being less inclined towards altruistic behavior.

***B. Study 2: The Effect of Empathy and the Formation Method on Behavior Toward the Struggling Party***

In this study, our aim was to further examine the impact of empathy on behavior by enhancing empathy elicitation. Furthermore, we sought to investigate the influence of the formation-of-contract method on people’s contractual behavior. Arguably, the more formal and legally binding a contract appears to people, the more likely their behavior will align with legal obligations. Conversely, when a contract is less formal, moral considerations may play a greater role in determining behavior. To test this hypothesis, we manipulated the contract formation process in our study.

**1. Participants**

Two hundred participants from the United States were recruited through Prolific and completed a pre-registered questionnaire online.[[70]](#footnote-71) Thirty-two participants who failed the attention check were excluded from the analysis. Of the remaining 168 participants, 84 were male, and 84 were female. The average age was 38.67 (SD = 14.1), 107 participants had some academic education, and the average Political Worldview score (on a scale from *0 = liberal*, to *100 = conservative*) was 33.3 (SD = 25.58).

**2. Procedure**

The experiment procedure was basically like that of Study 1, with four changes made to the legal scenario. First, to increase empathy for the business in the empathy elicitation condition, a more in-depth description of the harm it endured from the pandemic was provided. Second, in all versions, participants were presented with the *individual* condition. Third, we add a new independent variable of contract formation type. In the *formal* condition, a written contract was created by the sellers’ lawyer and clause 6(b) regarding the agreed compensation was presented to participants in a formal, legal manner. In the *informal* condition, there was no mention of a lawyer or written contract, and the scenario simply stated that the parties had agreed on the compensation. Fourth, participants were explicitly informed that according to the law, John is entitled to receive the agreed compensation of $1,000 (for the full text see Appendix A2).[[71]](#footnote-72)

**2. Results**

Thirty-three percent of the participants engaged in an economic maximization behavior, 52% in loss-avoidance behavior, and 14% demonstrated a loss-sharing behavior. As shown in Figure 2 and Table 3, there was a significant negative association between empathy elicitation and *Self-interest* behavior, and no significant association between empathy elicitation and *Loss-sharing* behavior. In addition, an association was found between contract formation and behavior. Thus, as depicted in Figure 3 and Table 3, under the *formal* condition participants were significantly more inclined to a *Self-interest* behavior, and significantly less inclined to a *Loss-sharing* behavior. No interaction effects of contract formation and empathy elicitation on either *Self-interest* or *Loss-sharing* were found.

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| **Table 3:** *Logistic Regression Analysis of The Effect of Empathy and Contracting Party on Behavior in Study 2* (N=168) |
|  | **DV: *Self-interest***  | **DV: *Loss-sharing***  |
|  | **M1** | **M2** | **M3** | **M1** | **M2** | **M3** |
| Empathy Elicitation | -0.66\* |  | -1.07\*\* | -0.07 |  | -0.08 |
| Formation |  | -0.92\*\* | -1.19\*\* |  | 1.02\* | 1.07\* |
| Empathy Scale |  |  | -0.31\* |  |  | 0.44 |
| Political Worldview |  |  | 0.01 |  |  | 0 |
| Academic Training |  |  | -0.07 |  |  | 1.5\* |
| Age  |  |  | -0.02 |  |  | 0.01 |
| Female |  |  | -0.39 |  |  | 0.85 |
| **R2** | 0.01 | 0.03 | 0.12 | 0 | 0.03 | 0.15 |
| + *p* < 0.1. \* *p* < 0.05. \*\* *p* < 0.01. \*\*\* *p* < 0.001. |

Table 4 reveals that a large portion of those who reported avoiding harm and exhibiting loss-sharing behavior believed that they were not legally bound to do so (77% and 87% respectively). Furthermore, half of those demonstrating loss-avoidance and a majority of those showing loss-sharing behavior (61%) thought that their actions should not be required by law.

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| **Table 4:** *Participants Reported Behavior by Their Expected Judgment and Personal Attitude in Study 2* (N=168) |
|  | **Expected Judgment** | **Desirable Judgment** |
|  | **S.I.** | **L.A.** | **L.S.** | **S.I.** | **L.A.** | **L.S.** |
| **Self-interest** | 86% | 12% | 2% | 89% | 11% | 0% |
| **Loss-avoidance** | 77% | 20% | 2% | 50% | 47% | 3% |
| **Loss-sharing**  | 48% | 39% | 13% | 22% | 39% | 39% |

**4. General Discussion**

Study 2 also shows that most participants behave altruistically and do not ask for the agreed compensation, even if they believe they are legally entitled to this compensation. Additionally, 14% of the participants in Study 2 reported that they would agree to absorb some of the losses they incurred to help the other struggling party.

 Contrary to Study 1, the empathy elicitation significantly reduced *Self-interest* behavior, showing that contractual empathy affects the degree of altruistic behavior. Additionally, the association between the manner of contract formation and altruistic behavior demonstrates that engaging in a formal relationship decreases the empathetic inclinations.

Both studies share several limitations. The first limitation pertains to external validity. Merely because most participants expressed their intention to behave altruistically and refrain from maximizing their compensation does not necessarily translate to real-life actions. On the one hand, it is one thing to say you are a nice guy and another thing to be one, so our findings might potentially overstate altruistic behavior. On the other hand, people may express an intention to take legal action, but when faced with the need to follow through, they might not do so. Therefore, the specific percentage of participants claiming altruistic behavior cannot be considered an accurate estimate of actual conduct. Nevertheless, it does suggest that such behavior is anticipated to be noteworthy, even if not to the same extent for every participant. Additionally, while the magnitude of the effect may vary, the anticipated direction of the impact stemming from the type of contractual party and contract formation is expected to remain consistent.

Another limitation pertains to the issue of generalizability. The specific circumstances leading to economic hardship for the company in the vignettes are distinctive. COVID-19 represents an idiosyncratic event experienced globally, resulting in widespread economic consequences. While we acknowledge the challenge of directly extrapolating behavior from difficulties arising from COVID-19 to other challenges in contract performance, it does underscore the significant role empathy plays in contractual behavior. It is reasonable to anticipate that empathy will influence behavior in different contexts, albeit to varying extents.

The second limitation concerns the reason underlying people exhibiting altruistic behavior. Our findings may suggest that people behaved altruistically due to empathy. Study 2 establishes a causal relationship between empathy elicitation and behavior. Furthermore, the contracting party and the contract formation were correlated with the empathy score. Thus, the casual relations that were found between these factors and behavior also indicate that empathy prompted participants’ reported behavior. However, in Study 1, the empathy manipulation did not impact behavior, raising the possibility that behavior affected the empathy score rather than vice versa. Additionally, at least part of the variance in behavior could be attributed to factors other than empathy. For instance, people might have felt compelled to assist the struggling party even without empathizing with them. An entirely different mechanism prompting participants’ behavior could be linked to administrative burden.

Thus, it might be the case that participants had an aversion to protecting their rights in courts due to administrative burden-related concerns. Administrative burdens are construed as imposing three distinct yet interconnected categories of costs: learning, compliance, and psychological costs.[[72]](#footnote-73) Learning costs pertain to the process by which individuals acquire the necessary knowledge to navigate procedural intricacies. Compliance costs are associated with obtaining requisite documentation and fulfilling financial obligations, while psychological costs encompass factors such as stigma, stress, and frustration. Hence, we cannot rule out the option that independent of empathy felt towards their contractual parties, aversion to costly and unpleasant bureaucratic procedures has led our participants to agree to compromise.[[73]](#footnote-74)

Finally, we cannot dismiss the possibility that individuals who claimed they would act to avoid losses might have been influenced by the compromise effect, leading them to opt for a middle-of-the-road alternative.[[74]](#footnote-75)

**V. Normative Implications**

Thus far, we have elucidated the dual nature of empathy, highlighting its advantages and associated risks. Also, we have observed that contractual parties exhibit varying degrees of empathy across different contexts. However, the implications for legal policy remain intricate, contingent upon diverse factors that vary in different contexts. While our objective is not to provide a definitive policy, this chapter endeavors to unfold the multifaceted considerations surrounding two policy inquiries: the prospect of increasing empathy through the expressive function of the law and enhancing pro-social behavior through the coercive function of the law.

**1. Increasing empathy**

Most people were empathetic to the struggling party in our studies, however, a noteworthy proportion did not exhibit altruistic behavior—42% in Study 1 and 53% in Study 2. Can this be altered? Empathy is first and foremost an issue of education, whether in schools, communities, or at home. Hence, fostering empathy can be achieved through educational initiatives. Strengthening social connections within business communities could also enhance empathy.[[75]](#footnote-76) Another avenue involves utilizing legal mechanisms, where legal rules impact the extent of empathy individuals feel for one another through the expressive function of the law. Individuals’ preferences are intertwined with legal frameworks, and the law holds the capacity to mold individual preferences, attitudes, and values.[[76]](#footnote-77) Consequently, the law may possess the potential to enhance empathy and consequently promote pro-social conduct even in the absence of legal sanctions. While the idea of creating a more empathetic world holds evident merit, it also holds some risks.

 ***The optimal level of empathy.*** Determining the optimal level of empathy presents a nuanced challenge. As previously discussed, empathy offers advantages such as facilitating cooperation, encouraging renegotiation, promoting efficient and fair loss-sharing, and enhancing social capital more broadly. However, empathy is not without its drawbacks. It can be exploited, leading individuals to take inefficient risks, impose undue costs on empathetic parties, and lead to unfair loss-sharing. Unjust distributive outcomes may also arise, with empathetic parties bearing disproportionate losses compared to their unempathetic counterparts. Finally, empathy generates negative emotions that, at least in certain instances, we would wish to avoid.

Consequently, establishing the ideal level of empathy becomes a complex task. Intervening in people’s emotions requires a grounded approach based on evidence. If accuracy in emotion manipulation cannot be assured, refraining from intervention may be the prudent course of action. The challenge extends beyond a lack of knowledge about the desired magnitude of induced empathy; it involves an inherent inability to predict how various means of influence will impact empathy in society. The effects of legal mechanisms on preferences are intricate, challenging to anticipate, and contingent upon context.[[77]](#footnote-78)

***Playing with people’s emotions.*** Manipulating people’s emotions requires careful consideration. Even if we possessed knowledge about the optimal level of empathy in specific cases and could accurately predict the outcomes of our subtle interventions, given how complex and hard to predict are the functioning of emotion in a collective institutional context,[[78]](#footnote-79) the impact of negative emotions varies among individuals. Even if empathy yields positive externalities and overall benefits empathetic individuals, there are instances where these negative emotions may not serve the well-being of the individual experiencing them. This could potentially lead to exploitation, as individuals might stage a distressing situation to leverage someone’s empathy. Therefore, to justify interventions that induce empathy, we must weigh whether the overall increase in social welfare justifies the potential harm to specific individuals for whom empathy does not serve their best interests.

***Risk of becoming a social norm.*** In addition, if empathy becomes the norm rather than the exception, this might create pressure on contractual parties to forgive unjustified breaches.[[79]](#footnote-80) In other words, we were originally trying to examine the benefit to society, where people when recognizing that enforcing the contract as it is, might show flexibility towards the party to the contract when the circumstances justify it. The creation of a social norm will create expectations for such forgiveness every time.[[80]](#footnote-81) when this becomes the norm, it will reduce the social meaning of empathy and kindness which will become just doing what one was expected to do.[[81]](#footnote-82)

**2. Mandate compassionate behavior**

Utilizing the law to promote empathy is just one way to foster pro-social behavior. An alternative approach involves making such behavior obligatory. Currently, there are legal rules that, in practice, necessitate parties to exhibit consideration toward the other party when encountering challenges in contract performance, excusing them from contractual obligations in certain instances. However, the question arises: is it advantageous to enforce mandatory consideration, and should we intensify or relax such requirements? Like the ambiguity surrounding the optimal level of empathy, determining the ideal degree of considerate behavior is complex. Yet, disparities exist between augmenting empathy and mandating compassionate behavior, necessitating careful consideration when mandating pro-social conduct when difficulties in performing the contract emerge.

 ***The advantages of the voluntary nature of empathy.*** As explained in Section III, the benefits derived from empathetic behavior are closely tied to its voluntary nature. In disputes arising from contractual conflicts, parties typically possess more pertinent information about the dispute, the breach, and the involved parties than judges and certainly more than legislators. Consequently, the parties are better positioned to discern whether to demonstrate compassionate behavior and to what extent. For instance, a party involved in a dispute is more likely to identify false representations of dire situations than the court. Furthermore, the positive effects that increased empathy brings to social capital, trust, renegotiations, and cooperation are predominantly attributable to the voluntary nature of the behavior. Altruistic actions resulting from genuine empathy contribute to these outcomes. Conversely, when compelled to act “compassionately”, the other party perceives it not as an altruistic gesture to which they are not entitled, but as a right they deserve, akin to any other contractual entitlement.

Moreover, when the promisee’s compassionate response is not assured, it is less likely for the promisor to take inefficient risks or unnecessarily breach the contract. Imposing mandatory rules that require overlooking breaches or exhibiting consideration makes it easier for cynical parties to exploit the situation. This, in turn, incentivizes actions that reduce expected social welfare.[[82]](#footnote-83)

 ***Reduces inequality between empathetic and non-empathetic people.*** Enforcing mandatory compassionate behavior offers an advantage in mitigating the unjust disparity between empathetic and non-empathetic individuals. As elucidated earlier, in a voluntary system, individuals who lack concern for others do not bear the financial burdens of struggling parties. This dynamic ultimately results in the transfer of wealth from empathetic to non-empathetic parties. Conversely, by imposing a uniform standard of compassionate conduct on everyone, the potential for this wealth transfer is alleviated.

 ***Crowding out.*** Finally,addressing the potential merits and drawbacks of including empathy requirements in contracts, we must also consider a behavioral aspect associated with the crowding-out theory. This paradigm suggests that external incentives, such as legal sanctions, can displace intrinsic motivations, such as empathy. Consequently, making compassionate behavior mandatory could potentially lead individuals to feel different about their compassionate actions (in terms of attribution, how rewarding it is, etc) and, in turn, reduce their motivation to behave compassionately. This theory presents an opposing prediction to the positive effects of mandating empathy, as advocated by expressive law theories that highlight law’s constructive impact of law as strengthening rather than disrupting pre-existing social norms and values.

In an attempt to answer this question in the context of mandating procedural justice in an organization, Feldman and Tyler[[83]](#footnote-84) have compared empirically the two approaches and found out that at least with regard to procedural justice, the effect of mandating voice procedure was associated with greater satisfaction by employees. Nonetheless, this finding, is not necessarily helpful in the context of mandating contractual empathy. In this context, we focus on the effect of the law, not on the recipient of the procedural justice or empathy but rather on the contracting party who debates how they themselves want to behave towards the other contracting party.

Understanding which prediction is likely to be stronger is indeed complex. What might be important to account for when attempting to understand how strong the crowding-out effect is likely to be in contractual contexts is to understand what behavioral mechanisms drives of crowding-out. Elsewhere, one of us[[84]](#footnote-85) has offered a taxonomy of nine types of crowding out processes divided into two main categories, behavioral and social. In the behavioral category, one can find for example over-justification for doing the right thing[[85]](#footnote-86) thus shifting the attention from the other party to compliance with the law[[86]](#footnote-87) control and trustworthiness which is being harmed when one does it because it’s the law[[87]](#footnote-88) ;harming the spontaneity of social behavior[[88]](#footnote-89) and harming the creation of cognitive dissonance.[[89]](#footnote-90) While in the social aspects of crowding out, we can account for decline in virtue signaling[[90]](#footnote-91) as was evident in the negative effect of monetary incentives to increase the social virtue of whistle-blowing.[[91]](#footnote-92) The bureaucratization of behavior which might reduce the taste of people to do the right thing as they see fit[[92]](#footnote-93) reactance to what is being seen as intrusive and illegitimate intervention in the freedom of contracts[[93]](#footnote-94) (e.g. provocative effect of law[[94]](#footnote-95)) and making social relations into market ones (e.g. fine is a price[[95]](#footnote-96)). Accounting for the likelihood that these different mechanisms will happen if we mandate empathy in the contractual relationship, will help us determine whether transforming the process of spontaneous empathy into a legally obligation might inadvertently lead to a reduction in the empathy.

**V. Conclusion**

A *homo economicus* perspective predicts that individuals act in a self-interested manner, displaying a “man is wolf to man” behavior[[96]](#footnote-97). In the realm of the theoretical discussion of contractual relationships, self-interest often takes center stage. However, our empirical research challenges this prevailing assumption. Our study reveals that individuals frequently make contractual decisions based on other-regarding concerns rather than purely self-interested motives. When confronted with a contractual breach stemming from the partner’s difficulties, a substantial number of participants demonstrate a remarkable willingness to assist rather than exploit the struggling party. Remarkably, some even voluntarily relinquish contractual rights and absorb losses to aid the party that breached the contract. We contend that this behavior is significantly influenced by empathy and compassion, showing the importance of understanding the neglected role of empathy and compassion in contractual behavior.

Empathy, often underestimated in contract theory, emerges as a potent force within contractual relationships. Our findings highlighted its role in reducing transaction costs, promoting cooperation, and fostering equitable loss-sharing. However, this nuanced attribute also presents challenges. While empathetic tendencies enhance trust and collaboration, they simultaneously create openings for exploitation by cynical parties. Hence in this paper, we delve into the delicate balance between empathy’s benefits and potential pitfalls. We explore how heightened awareness of empathetic inclinations can lead to both fair outcomes and inefficiencies. Moreover, we examine the unwarranted allocation of resources and the unintended sentiments that empathy may evoke in commercial contexts.

The optimal role of empathy within the legal framework, especially in contract law, remains an open question. Should we fully embrace empathy, actively enhance it, or maintain a clear separation between its influence on human behavior and legal outcomes? This policy dilemma hinges on moral perspectives and empirical evidence. Our hope is that this paper contributes to the ongoing discourse, stimulating further research that refines how contract law grapples with the multifaceted role of empathy. Future empirical and legal research can contribute to crafting a more nuanced and effective legal framework—one that harmonizes compassion with sound contractual policies.

1. \* Ori Katz is an assistant professor at Bar Ilan University and Yuval Feldman is the Mori Lazarof Professor of Law and Associate Dean for Research. For valuable comments on previous drafts, we are grateful to Shoham Choshen-Hillel, Eyal Zamir … and the participants of the Chicago/Michigan Psychology and Law Studies group and of the Law and Economic Workshop at The Hebrew University. We thank Shira Gelb for her excellent research assistance. The study was supported by ERC Grant number: 101054656 / Project acronym: VCOMP. [↑](#footnote-ref-2)
2. *See*, *e.g,* Louis Kaplow & Steven Shavell, *Fairness versus welfare* (Cambridge, MA : Harvard University Press, 2002) at 155; Tore Ellingsen & Magnus Johannesson, “Promises, Threats and Fairness” (2004) 114:495 The Economic Journal 397–420 at 397. [↑](#footnote-ref-3)
3. Elizabeth S Anderson & Richard H Pildes, “Expressive Theories of Law: A General Restatement” (1999) 148:5 U Pa L Rev 1503–1576; Richard H McAdams, *The Expressive Powers of Law: Theories and Limits* (Harvard University Press, 2015); Cass R Sunstein, “On the Expressive Function of Law” (1995) 144:5 U Pa L Rev 2021–2054. [↑](#footnote-ref-4)
4. Christoph Vanberg, “Why Do People Keep Their Promises? An Experimental Test of Two Explanations” (2008) 76:6 Econometrica 1467–1480 at 1467–1468. [↑](#footnote-ref-5)
5. C Daniel Batson et al, “Empathic Joy and the Empathy-Altruism Hypothesis” (1991) 61:3 Journal of Personality and Social Psychology 413–426 at 413. [↑](#footnote-ref-6)
6. Generally, transactional contracts are short-term and specific, such as placing an order with a supplier, while relational contracts are characterized by long-term commitments and a high level of trust between the parties, for instance, parents enrolling their child in daycare. *See*, *e.g.* David Frydlinger et al, “A Comparison of Transactional and Relational Contract Models” in David Frydlinger et al, eds, *Contracting in the New Economy: Using Relational Contracts to Boost Trust and Collaboration in Strategic Business Relationships* (Cham: Springer International Publishing, 2021) 93. [↑](#footnote-ref-7)
7. See below the text accompanied by *supra* note 31. [↑](#footnote-ref-8)
8. See below the text accompanied by *supra* notes 33-39. [↑](#footnote-ref-9)
9. See below the text accompanied by *supra* notes 39-41. [↑](#footnote-ref-10)
10. See below the text accompanied by *supra* notes 43-51. [↑](#footnote-ref-11)
11. See below the text accompanied by *supra* notes 50-55. [↑](#footnote-ref-12)
12. Bloom, Paul. *Against Empathy: The Case for Rational Compassion*. Random House, 2017. [↑](#footnote-ref-13)
13. See below the text accompanied by *supra* note 60. [↑](#footnote-ref-14)
14. Lisa Bernstein, “Opting out of the Legal System: Extralegal Contractual Relations in the Diamond Industry” (1992) 21:1 The Journal of Legal Studies 115–157; Tess Wilkinson-Ryan, “Legal Promise and Psychological Contract Essay” (2012) 47 Wake Forest L Rev 843–874 at 863–865. [↑](#footnote-ref-15)
15. Benjamin Klein & Keith B Leffler, “The Role of Market Forces in Assuring Contractual Performance” (1981) 89:4 Journal of Political Economy 615–641; George Baker, Robert Gibbons & Kevin J Murphy, “Subjective Performance Measures in Optimal Incentive Contracts\*” (1994) 109:4 The Quarterly Journal of Economics 1125–1156; Jonathan Levin, “Relational Incentive Contracts” (2003) 93:3 American Economic Review 835–857. [↑](#footnote-ref-16)
16. Joyce Berg, John Dickhaut & Kevin McCabe, “Trust, Reciprocity, and Social History” (1995) 10:1 Games and Economic Behavior 122–142; Noel D Johnson & Alexandra A Mislin, “Trust games: A Meta-Analysis” (2011) 32:5 Journal of Economic Psychology 865–889. [↑](#footnote-ref-17)
17. Gary Charness & Martin Dufwenberg, “Promises and Partnership” (2006) 74:6 Econometrica 1579–1601. [↑](#footnote-ref-18)
18. Vanberg, “Why Do People Keep Their Promises?”, *supra* note 3. [↑](#footnote-ref-19)
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20. Florian Ederer & Alexander Stremitzer, “Promises and Expectations” (2017) 106 Games and Economic Behavior 161–178; Dorothee Mischkowski, Rebecca Stone & Alexander Stremitzer, “Promises, Expectations, and Social Cooperation” (2019) 62:4 The Journal of Law and Economics 687–712. [↑](#footnote-ref-21)
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22. Tania Singer & Nikolaus Steinbeis, “Differential Roles of Fairness- and Compassion-Based Motivations for Cooperation, Defection, and Punishment” (2009) 1167:1 Annals of the New York Academy of Sciences 41–50 (contrasting between fairness-based and compassion-based motivations, and empirically demonstrating the advantages and disadvantages of both motivations in the context of cooperation) ; In theory, if individuals view contractual promises as commitments to exert their best efforts, then when the promisor is without fault, there is no breach of the contract, and it should not erode trust between the parties. However, in situations where individuals perceive obligations as guaranteeing a specific outcome, or if they believe the promisor is at fault for the breach, a reduction in trust is anticipated. See Richard A. Epstein, The Many Faces of Fault in Contract Law: Or How to Do Economics Right, Without Really Trying, 107 Mich. L. Rev. 1461 (2009); George M. Cohen, *The Fault That Lies within Our Contract Law*, 107 Mich. Law Rev. 1445 (2008) (arguing that fault plays an inherent part within the framework of contract law), and see also below note 30. [↑](#footnote-ref-23)
23. Batson et al, *supra* note 4; Inbal Ben-Ami Bartal, Jean Decety & Peggy Mason, “Empathy and Pro-Social Behavior in Rats” (2011) 334:6061 Science 1427–1430; Shoham Choshen-Hillel et al, “Physicians prescribe fewer analgesics during night shifts than day shifts” (2022) 119:27 Proceedings of the National Academy of Sciences e2200047119; Jean Decety et al, “Empathy as a Driver of Prosocial Behaviour: Highly Conserved Neurobehavioural Mechanisms Across Species” (2016) 371:1686 Philosophical Transactions of the Royal Society B: Biological Sciences 20150077; Tom Gordon-Hecker et al, “Empathy for the Pain of Others: Sensitivity to the Individual, Not to the Collective” (2024) 110 Journal of Experimental Social Psychology 104561.

Martin L. Hoffman, *Empathy and Prosocial Behavior*, 3 HANDBOOK OF EMOTIONS 440 (2008) [↑](#footnote-ref-24)
24. Mark H Davis, “Empathy, Compassion, and Social Relationships” in Emma M Seppälä et al, eds, *The Oxford Handbook of Compassion Science* (Oxford University Press, 2017) 0 at 300. [↑](#footnote-ref-25)
25. *Ibid* at 303–304. [↑](#footnote-ref-26)
26. Paul Ekman & Eve Ekman, “Is Global Compassion Achievable?” in Emma M Seppälä et al, eds, *The Oxford Handbook of Compassion Science* (Oxford University Press, 2017) 0 at 41–43. [↑](#footnote-ref-27)
27. This is an example of a relational contract, that is expected to yield a higher sense of empathy, cf. supra note 4, above. Nevertheless, transactional contracts could also elicit empathy as demonstrated in our empirical findings in Section IV below. [↑](#footnote-ref-28)
28. Klimecki, Olga, et al. "Empathy Promotes Altruistic Behavior in Economic Interactions". Scientific Reports, vol. 6, no. 1, 2016. https://doi.org/10.1038/srep31961 [↑](#footnote-ref-29)
29. Ori Katz, “Mapping the Diversity of Thought - An Attitude Theory of Contract Law” (2021) 31:1 S Cal Interdisc LJ 49–90 at 59–62. [↑](#footnote-ref-30)
30. See e.g. Wallach, George (1979) “Excuse Defense in the Law of Contracts: Judicial Frustration of the U.C.C. Attempt to Liberalize the Law of Commercial Impracticability,” 55 Notre Dame Law Review 203. Wladis, John D. (1986) “Common Law and Uncommon Events: The Development of the Doctrine of Impossibility of Performance in English Contract Law,” 75 Georgetown Law Journal 1575; Melvin A. Eisenberg, *Impossibility, Impracticability, and Frustration*, 1 J. Leg. Anal. 207, 208 (2009); John D. Wladis, Common Law and Uncommon Events: The Development of the Doctrine of Impossibility of Performance in English Contract Law, 75 GEO. L.J. 1575 (1987) [↑](#footnote-ref-31)
31. Andrew A Schwartz, “Contracts and COVID-19 Essay” (2020) 73 Stan L Rev Online 48–60 at 49.
This does not imply that contracts inherently establish strict liability, which is often not the case. *See*, *e.g.*, George M. Cohen, *The Fault That Lies within Our Contract Law*, 107 Mich. Law Rev. 1445 (2008); Robert A. Hillman, *The Future of Fault in Contract Law Drafting Our Future: Contract Law in 2025*, 52 Duquesne Law Rev. 275 (2014); Omri Ben-Shahar & Ariel Porat, *Foreword: Fault in American Contract Law*, 107 Mich. Law Rev. 1341, 1342-1343 (2009). Nonetheless, often parties are expected to fulfill the contract even when it is challenging, and fault is not always necessary to establish contractual liability. [↑](#footnote-ref-32)
32. Tess Wilkinson-Ryan & Jonathan Baron, “Moral Judgment and Moral Heuristics in Breach of Contract” (2009) 6 J Empirical Legal Stud 405–424; Uriel Haran, “A Person-Organization Discontinuity in Contract Perception: Why Corporations Can Get Away with Breaking Contracts but Individuals Cannot” (2013) 59:12 Management Science 2837–2853. Haran, Uriel, Doron Teichman, and Yuval Feldman. "Formal and Social Enforcement in Response to Individual Versus Corporate Transgressions." *Journal of Empirical Legal Studies* 13.4 (2016): 786-808. [↑](#footnote-ref-33)
33. However, empathy can serve as a signal to the promisor, potentially leading them to perceive a legal entitlement to breach the contract. This increased perception of entitlement may elevate the likelihood of pursuing litigation. For example, if the teacher received half the payment without any legal action, she might believe she is entitled to the entire sum. [↑](#footnote-ref-34)
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36. Scott, Robert E. "Conflict and Cooperation in Long-Term Contracts." *Calif. L. Rev.* 75 (1987): 2005. [↑](#footnote-ref-37)
37. Peter Oomsels et al., *Functions and Dysfunctions of Interorganizational Trust and Distrust in the Public Sector*, 51 Adm. Soc. 516 (2019); Koen Verhoest, Martino Maggetti, Bastiaan Redert, *Strengthening Trust by Design* **preliminary draft, do not cite yet** (“too much trust can become ‘blind trust’, allowing the trustee to behave opportunistically”) [↑](#footnote-ref-38)
38. Batson, C. D., & Moran, T. (1999). Empathy-Induced Altruism in a Prisoner’s Dilemma. European Journal of Social Psychology, 29(7), 909–924. https://doi.org/10.1002/(SICI)1099-0992(199911)29:7<909:: AID-EJSP965>3.0.CO;2-L [↑](#footnote-ref-39)
39. Batson, C. D., & Ahmad, N. (2001). Empathy-Induced Altruism in a Prisoner’s Dilemma II: What if the Target of Empathy Has Defected? European Journal of Social Psychology, 31(1), 25–36. https://doi.org/ 10.1002/ejsp.26 [↑](#footnote-ref-40)
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43. Dreber et al, *supra* note 34. [↑](#footnote-ref-44)
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69. To assess the participants’ perspectives on contracts as either business transactions or promises, we utilized two methods of assessment. The first was an implicit measurement using the word fragment completion task, introduced by Uriel Haran (2013), and the second was an explicit measurement consisting of six statements. However, due to the low reliability of both measurements (α=0.44, 0.51 respectively), they were not included in the analysis. [↑](#footnote-ref-70)
70. See pre-registration for Study 2 here: <https://aspredicted.org/LSC_4HY>. [↑](#footnote-ref-71)
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75. *See, e.g.,* Bernstein, “Opting out of the Legal System”, *supra* note 12. [↑](#footnote-ref-76)
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